

Avon Rubber

Hitting the numbers

Avon Rubber's pre-close has confirmed that the group will meet market expectations and that performance in H217 has continued apace. With positive mix effects in Protection & Defence and continued strengthening in Dairy, we believe that the eventual revenue and margin mix may alter slightly but that our profit levels will be achieved. With CEO Paul McDonald signalling continued confidence into 2018 and with further medium-term product developments to come through in both divisions, we continue to view Avon as delivering in the short and medium term.

Year end	Revenue (£m)	PBT* (£m)	EPS* (p)	DPS (p)	P/E (x)	Yield (%)
09/15	134.3	19.8	56.1	7.3	16.9	0.8
09/16	142.9	21.6	74.2	9.5	12.8	1.0
09/17e	168.9	25.0	66.6	11.0	14.3	1.2
09/18e	178.7	26.9	71.4	13.0	13.3	1.4

Note: *PBT and EPS are normalised, excluding amortisation of acquired intangibles, exceptional items and share-based payments.

Positive trends in both divisions

The pre-close statement showed that both the Protection & Defence (P&D) and Dairy divisions continued to progress positively. In P&D, 152,000 mask systems and 144,000 spare filter pairs are expected to be delivered, while the flexibility in the group means it will be able to fulfil the May 2017 order for 37,000 FM50 general purpose masks in the current financial year, with a consequential benefit to mix. Likewise, the supportive market environment in Dairy has allowed the positive growth trends seen in the division to continue into H2 with a particularly pleasing performance from InterPuls, which had previously been more affected by capital spend delays in the sector.

Delivering profit, cash and embedded growth

Avon has again highlighted its ability to deliver consistently, both in terms of profit and strong cash generation. With recent years' investments also set to drive further growth over the coming years, we maintain our view that Avon has the market position, product portfolio and ambition to further accelerate its growth through organic and inorganic means. The confirmation of trading in line with expectations is positive in our view and demonstrates the robust nature of the group, even during the period of management change. We expect the new management team now in place to progressively stamp its own authority and signature on the group.

Valuation: Opportunity following pause?

Following a period of consolidation, Avon Rubber is currently trading on just 13.3x FY18e EPS compared to its aerospace and defence peers, which are trading on an average of 17.1x. We believe that the confirmation of in-line trading at the pre-close, in conjunction with the higher than average growth rates, should justify a return to premium ratings, as previously witnessed. With confidence signalled in the order pipeline and further growth prospects, which we will revisit alongside results, we continue to believe that Avon has further medium-term upside earnings potential.

Pre-close statement

Aerospace & defence

15 September 2017

Price **950p**

Market cap **£295m**

\$1.29/£

Net cash (£m) at 31 March 2017 12.6

Shares in issue 31.0m

Free float 96%

Code AVON

Primary exchange LSE

Secondary exchange N/A

Share price performance



% 1m 3m 12m

Abs (5.0) (6.3) 0.5

Rel (local) (4.3) (4.1) (8.5)

52-week high/low 1,119p 930p

Business description

Avon Rubber designs, develops and manufactures products in the respiratory protection, defence (71% of 2016 sales) and dairy (29%) sectors. Its major contracts are with national security and safety organisations such as the DoD. 86% of sales are from the US and 14% are from Europe.

Next events

FY17 results 15 November 2017

Analysts

Roger Johnston +44 (0)20 3077 5722

Annabel Hewson +44 (0)20 3077 5700

Andy Chambers +44 (0)20 3681 2525

industrials@edisongroup.com

[Edison profile page](#)

Avon Rubber is a research client of Edison Investment Research Limited

Exhibit 1: Financial summary

Year end 30 September	£000s	2013	2014	2015	2016	2017e	2018e
PROFIT & LOSS							
Revenue		124,851	124,779	134,318	142,884	168,853	178,654
Cost of Sales		(91,140)	(83,264)	(88,618)	(90,159)	(106,545)	(112,730)
Gross Profit		33,711	41,515	45,700	52,725	62,308	65,924
EBITDA		20,440	23,164	26,586	30,808	35,718	36,873
Operating Profit (before amort. and except.)		14,223	17,003	20,215	21,763	25,190	27,055
Amortisation of Intangibles		(417)	(261)	(1,043)	(3,307)	(3,000)	(3,024)
Exceptionals		(383)	(2,017)	(604)	(506)	0	0
Other		(420)	(400)	318	(320)	(400)	(400)
Operating Profit		13,003	14,325	18,886	17,630	21,790	23,631
Net Interest		(347)	(274)	(147)	(154)	(150)	(150)
Other finance costs		(253)	(187)	(247)	(33)	0	0
Profit Before Tax (norm)		13,656	16,554	19,821	21,576	25,040	26,905
Profit Before Tax (FRS 3)		12,403	13,864	17,838	16,801	21,640	23,481
Tax		(3,566)	(3,053)	(2,672)	1,824	(4,869)	(5,283)
Tax adjustment		(122)	(450)	(253)	(924)	0	0
Profit After Tax (norm)		9,968	13,051	16,896	22,476	20,171	21,622
Profit After Tax (FRS 3)		8,837	10,811	15,166	18,625	16,771	18,198
Average Number of Shares Outstanding (m)		29.5	29.9	30.1	30.3	30.3	30.3
EPS - normalised (p)		33.8	43.7	56.1	74.2	66.6	71.4
EPS - continuing, FRS 3 (p)		30.0	36.2	50.4	61.5	55.4	60.1
DPS (p)		4.3	5.6	7.3	9.5	11.0	13.0
Gross Margin (%)		27%	33%	34%	37%	37%	37%
EBITDA Margin (%)		16%	19%	20%	22%	21%	21%
Operating Margin (before amort. and except.) (%)		11%	14%	15%	15%	15%	15%
BALANCE SHEET							
Fixed Assets		36,928	36,815	74,095	85,244	81,639	79,146
Intangible Assets		16,541	17,240	41,309	47,357	47,734	48,283
Tangible Assets		20,387	19,575	28,212	30,112	26,130	23,088
Other		0	0	4,574	7,775	7,775	7,775
Current Assets		34,449	34,971	34,481	45,111	59,828	78,330
Stocks		13,374	12,887	17,123	20,648	19,811	20,960
Debtors		20,891	19,159	17,026	19,968	20,938	22,153
Cash		184	2,925	332	4,495	19,080	35,216
Assets held for sale		0	0	0	0	0	0
Current Liabilities		(23,369)	(26,453)	(27,178)	(36,641)	(32,652)	(33,970)
Creditors		(17,296)	(19,601)	(18,005)	(24,185)	(22,695)	(24,013)
Short term borrowings		0	0	(2,350)	(2,499)	0	0
Tax		(6,073)	(6,852)	(6,823)	(9,212)	(9,212)	(9,212)
Other		0	0	0	(745)	(745)	(745)
Long Term Liabilities		(27,312)	(20,317)	(39,194)	(51,713)	(51,713)	(51,713)
Long term borrowings		(11,059)	0	(11,143)	0	0	0
Deferred Tax		(2,977)	(2,315)	(9,734)	(10,007)	(10,007)	(10,007)
Retirement benefit obligations		(11,279)	(16,029)	(16,605)	(39,951)	(39,951)	(39,951)
Provisions		(1,997)	(1,973)	(1,712)	(1,755)	(1,755)	(1,755)
Other		0	0	0	0	0	0
Net Assets		20,696	25,016	42,204	42,001	57,102	71,793
CASH FLOW							
Operating Cash Flow		14,708	25,004	20,446	31,680	32,896	34,225
Net Interest		(364)	(314)	(147)	(309)	(150)	(150)
Tax		(2,229)	(2,903)	(3,270)	(1,031)	(4,869)	(5,283)
Capex		(11,054)	(6,815)	(6,183)	(6,838)	(6,923)	(7,325)
Acquisitions/disposals		(437)	(31)	(21,228)	(3,250)	0	0
Equity financing		(1,765)	0	(1,152)	(1,812)	(1,000)	(2,000)
Dividends		(1,132)	(1,422)	(1,859)	(2,430)	(2,870)	(3,330)
Net Cash Flow		(2,273)	13,519	(13,393)	16,010	17,084	16,136
Opening net (debt)/cash		(8,725)	(15,937)	2,925	(13,161)	1,996	19,080
Cash FX effect		123	281	97	(853)	0	0
Discontinued operations / relocation		0	0	0	0	0	0
Debt FX and Other		(5,062)	5,062	(2,790)	0	0	0
Closing net (debt)/cash		(15,937)	2,925	(13,161)	1,996	19,080	35,216

Source: Company accounts, Edison Investment Research

Edison is an investment research and advisory company, with offices in North America, Europe, the Middle East and AsiaPac. The heart of Edison is our world-renowned equity research platform and deep multi-sector expertise. At Edison Investment Research, our research is widely read by international investors, advisers and stakeholders. Edison Advisors leverages our core research platform to provide differentiated services including investor relations and strategic consulting. Edison is authorised and regulated by the [Financial Conduct Authority](#). Edison Investment Research (NZ) Limited (Edison NZ) is the New Zealand subsidiary of Edison. Edison NZ is registered on the New Zealand Financial Service Providers Register (FSP number 247505) and is registered to provide wholesale and/or generic financial adviser services only. Edison Investment Research Inc (Edison US) is the US subsidiary of Edison and is regulated by the Securities and Exchange Commission. Edison Investment Research Limited (Edison Aus) [46085869] is the Australian subsidiary of Edison and is not regulated by the Australian Securities and Investment Commission. Edison Germany is a branch entity of Edison Investment Research Limited [4794244]. www.edisongroup.com

DISCLAIMER

Copyright 2017 Edison Investment Research Limited. All rights reserved. This report has been commissioned by Avon Rubber and prepared and issued by Edison for publication globally. All information used in the publication of this report has been compiled from publicly available sources that are believed to be reliable, however we do not guarantee the accuracy or completeness of this report. Opinions contained in this report represent those of the research department of Edison at the time of publication. The securities described in the Investment Research may not be eligible for sale in all jurisdictions or to certain categories of investors. This research is issued in Australia by Edison Aus and any access to it, is intended only for "wholesale clients" within the meaning of the Australian Corporations Act. The Investment Research is distributed in the United States by Edison US to major US institutional investors only. Edison US is registered as an investment adviser with the Securities and Exchange Commission. Edison US relies upon the "publishers' exclusion" from the definition of investment adviser under Section 202(a)(11) of the Investment Advisers Act of 1940 and corresponding state securities laws. As such, Edison does not offer or provide personalised advice. We publish information about companies in which we believe our readers may be interested and this information reflects our sincere opinions. The information that we provide or that is derived from our website is not intended to be, and should not be construed in any manner whatsoever as, personalised advice. Also, our website and the information provided by us should not be construed by any subscriber or prospective subscriber as Edison's solicitation to effect, or attempt to effect, any transaction in a security. The research in this document is intended for New Zealand resident professional financial advisers or brokers (for use in their roles as financial advisers or brokers) and habitual investors who are "wholesale clients" for the purpose of the Financial Advisers Act 2008 (FAA) (as described in sections 5(c) (1)(a), (b) and (c) of the FAA). This is not a solicitation or inducement to buy, sell, subscribe, or underwrite any securities mentioned or in the topic of this document. This document is provided for information purposes only and should not be construed as an offer or solicitation for investment in any securities mentioned or in the topic of this document. A marketing communication under FCA Rules, this document has not been prepared in accordance with the legal requirements designed to promote the independence of investment research and is not subject to any prohibition on dealing ahead of the dissemination of investment research. Edison has a restrictive policy relating to personal dealing. Edison Group does not conduct any investment business and, accordingly, does not itself hold any positions in the securities mentioned in this report. However, the respective directors, officers, employees and contractors of Edison may have a position in any or related securities mentioned in this report. Edison or its affiliates may perform services or solicit business from any of the companies mentioned in this report. The value of securities mentioned in this report can fall as well as rise and are subject to large and sudden swings. In addition it may be difficult or not possible to buy, sell or obtain accurate information about the value of securities mentioned in this report. Past performance is not necessarily a guide to future performance. Forward-looking information or statements in this report contain information that is based on assumptions, forecasts of future results, estimates of amounts not yet determinable, and therefore involve known and unknown risks, uncertainties and other factors which may cause the actual results, performance or achievements of their subject matter to be materially different from current expectations. For the purpose of the FAA, the content of this report is of a general nature, is intended as a source of general information only and is not intended to constitute a recommendation or opinion in relation to acquiring or disposing (including refraining from acquiring or disposing) of securities. The distribution of this document is not a "personalised service" and, to the extent that it contains any financial advice, is intended only as a "class service" provided by Edison within the meaning of the FAA (ie without taking into account the particular financial situation or goals of any person). As such, it should not be relied upon in making an investment decision. To the maximum extent permitted by law, Edison, its affiliates and contractors, and their respective directors, officers and employees will not be liable for any loss or damage arising as a result of reliance being placed on any of the information contained in this report and do not guarantee the returns on investments in the products discussed in this publication. FTSE International Limited ("FTSE") © FTSE 2017. "FTSE®" is a trade mark of the London Stock Exchange Group companies and is used by FTSE International Limited under license. All rights in the FTSE indices and/or FTSE ratings vest in FTSE and/or its licensors. Neither FTSE nor its licensors accept any liability for any errors or omissions in the FTSE indices and/or FTSE ratings or underlying data. No further distribution of FTSE data is permitted without FTSE's express written consent.